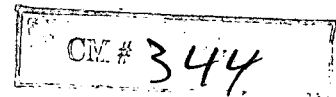




DEPARTMENT OF AGRICULTURE
OFFICE OF THE SECRETARY
WASHINGTON, D. C. 20250



January 27, 1983

MEMORANDUM FOR CABINET COUNCIL ON FOOD AND AGRICULTURE

FROM: John R. Block
Secretary of Agriculture

SUBJECT: Agricultural Credit Outlook

BACKGROUND

During the past 60 days, the news media have extensively reported on a number of farm sales which have been disrupted by a small group of farmers and rural residents. The reports suggest that the Federal Government is actively forcing out of business small family farmers through foreclosures and withdrawal of necessary operating credit.

Beginning in 1970, there has been a rapid increase in the total outstanding farm debt from \$54.5 billion to an estimated \$215 billion in 1983. As farmers expanded their operations and invested heavily in capital equipment, the lending community made credit readily available. This credit availability relied heavily on the rapidly inflating values of real estate which continued to rise during the decade before leveling off -- and beginning to show slight declines -- in 1981 and 1982. During this period, many lenders did not adequately supervise their loans. They frequently neglected to determine whether adequate repayment ability existed as producers expanded. In some regions of the country, principally the South and Southeast, changing cropping patterns and consecutive years of poor weather put further pressure on lenders for liberal lending standards to accommodate the financial needs of agricultural producers.

Beginning in 1977, the commercial and Farm Credit System lenders found it necessary to begin to review agricultural loan standards more carefully. However, at this same point, the Congress passed the Economic Emergency Act which provided unusually liberal lending standards for the Farmers Home Administration. This Act, coupled with a similar program in the Small Business Administration, produced a massive runup in Federal farm lending, substantial amounts of which were of poor quality and counter-productive to the best interests of the individual producer.

Thus, as the agricultural community entered the 1980's, marked by rapidly escalating interest rates and high inflation, the accumulation of large agricultural surpluses and depressed agricultural commodity prices, a small

but significant number of agricultural producers found themselves under major economic stress. Although actual numbers of foreclosures remain small, as a percentage they have more than doubled between 1981 and 1982 and appear to be holding at about 1982 levels or slightly higher as we move into the 1983 lending season.

Currently, delinquent accounts held by commercial and Farm Credit System lenders range from 2.5 to 3.9 percent of their portfolios. At the same time, the delinquent accounts of USDA's Farmers Home Administration, the lender of last resort, currently make up 24 percent of its portfolio of 268,000 borrowers. During 1982, completed foreclosures for the Farm Credit System, the largest agricultural lender, totaled approximately 1,200 while the Farmers Home Administration had 844. Commercial and Farm Credit System lenders are genuinely concerned about the trend they are experiencing. For example, the Farm Credit System's Production Credit Associations which provide short term credit to farmers, report that loan losses increased from \$22 million in 1981 to \$156 million in 1982. The 1982 figure represents 75 percent of the total losses which had been experienced by that System in its entire history prior to 1982. While the Farm Credit System anticipates a leveling off of this trend in 1983, commercial and Farm Credit System lenders have tightened their agricultural lending standards to require adequate repayment ability in addition to adequate security. This has placed additional pressure on the Government lending agency, Farmers Home Administration, to accommodate commercial lenders or assume additional agricultural loans directly. As a result, the total market share of Government agricultural lending by FmHA and CCC has risen dramatically through 1982 and will continue to rise in 1983. In total, the Government through FmHA and CCC will provide an all-time record level of short term credit to the farming community of approximately \$16 billion in 1983.

Although the actual number of producers facing serious financial difficulty is small, there is a public perception enhanced by the media that the problem is more widespread and serious than the record would support. This perception has led Congress four times in the last 18 months to attempt to pass some form of loan deferral legislation. These bills have had one common thread: they would allow, at the request of the farmer, a moratorium on loan repayments to FmHA for a period certain. USDA has aggressively opposed this type of legislative action. The Farm Bureau and leaders in various commodity organizations have indicated that the farming community strongly supports the position that each farmer's situation should be evaluated individually and that a general moratorium should not be granted. In the next few weeks, at least eight significant legislative proposals on agricultural credit can be expected to be introduced. Congressional Agricultural Committee leaders in the Congress, particularly the House, have indicated that they will concentrate their Congressional attention on the credit question during the next few months. Attachment 1 summarizes the most significant proposals being brought forward by Congress.

The major media outlets indicate significant continuing attention to this issue which will probably occur during the next 60 days, including segments being developed for "60 Minutes" and the major weekly news magazines.

USDA PLANNED ACTIONS

1. USDA implemented case-by-case lending guidelines in 1982 which gave broad discretion on an individual basis to assist borrowers under financial stress. During 1982, 40,000 of the 268,000 borrowers of FmHA received special consideration in the form of deferrals, reschedulings, the carrying of delinquent accounts or other actions to assist them to continue in operation. Of these 40,000 actions, 20,000 involved subordination of the Government's collateral position to commercial lenders so that the commercial and Farm Credit System could supply credit to their regular customers. USDA intends to continue to aggressively use these authorities through the 1983 lending season.
2. USDA's PIK program will reduce the total credit that is needed for production expenses in the year ahead and will thereby reduce some of the financial lending stress which producers are experiencing.
3. USDA intends to aggressively oppose general moratorium and deferment legislation, new lending schemes and any legislation which would lead to assumption of commercial sector poor lending risk. These types of lending policies are counter-productive in almost all cases to the interest of the individual producer. In addition, they lack the support of the general farming community and represent major budget impacts.
4. USDA will meet with agricultural financial lenders and farm commodity organization leaders on a regular basis during the balance of the lending season to monitor financial conditions and the severity of credit problems. This commitment to ascertain an accurate picture of credit conditions represents the continuation of an effort commenced by Secretary Block over a year ago.
5. USDA expects support from organizations such as the Farm Bureau for the Administration's opposition to general moratorium and deferral legislation. USDA will also undertake a campaign to inform its farm audiences and the media of the substantial actions taken by the Administration to demonstrate compassion and concern to the current problems faced by some producers.
6. USDA has issued guidelines which have been successfully used by the Farmers Home Administration's lending officials in effectively handling disruptive actions by a small number of militant rural residents and farmers in incidents involving farm sales. Similar training efforts in handling these situations will be undertaken by the Farm Credit Administration for its lenders next week. USDA, through the Cabinet Council on Food and Agriculture, will provide senior staff centralized information concerning farm foreclosure sales, bankruptcies, and loan delinquent rates for the balance of this lending season which ends in late April.

Prospective 1983 Legislative Proposals Affecting FmHAI Bills which have been introduced in the new session:

- A. H.R. 568 - Sponsor - Evans (Iowa) requires farmers to implement conservation plans as an eligibility prerequisite for FmHA loans to acquire or enlarge farms.
- B. H.R. 589 - Sponsor - Gore (Tennessee) permits FmHA to make emergency loans of up to \$5,000 on the basis of estimated farmer loss.
- C. H.R. 590 - Sponsor - Gore (Tennessee) reduces the disaster emergency loan rate to 5 percent for the amount of loss and the interest rate for other loan purposes to the cost of money instead of prevailing market rates.

II Probable additional legislative proposals which are expected to be introduced:

- A. Sponsor - Daschle (South Dakota) and Dorgan (North Dakota) - A general deferral moratorium bill closely resembling a comparable proposal of the last legislative session known as the Daschle Farm Crisis Bill.
- B. Sponsor - Alexander (Arkansas) - A bill providing for FmHA to guarantee (90 percent) any private farm loan that is considered to be high risk in nature, i.e., delinquent or nearing foreclosure. It further provides FmHA authority to buy up such guaranteed loans.
- C. Sponsor - Cochran (Mississippi) - A 1983 Farm Credit bill expected to be introduced this week. Cochran and others as sponsors are developing a broad based farm credit relief package which is expected to include proposals on deferral moratorium and additional lending authorities and higher loan size limits for FmHA.
- D. Sponsor - Huddleston (Kentucky) - A competing Democratically sponsored general farm bill with major farm credit sections aimed at FmHA as an alternative to the expected Cochran proposal.
- E. Sponsor - Pepper (Florida) - A general economic recovery bill is expected which will incorporate a farm loan repayment moratorium feature.
- F. Sponsor - Sasser (Tennessee) - A two-year loan deferral bill coupled with some modification of the economic emergency loan provision.

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III Administration proposal:

Congress did not complete action on reauthorization of the Consolidated Farm and Rural Development Act in the last session. The Agricultural Credit Subcommittee under Ed Jones is expected to develop a Congressional proposal. The Administration is preparing for transmittal an authorization proposal corresponding to the President's 1984 budget request and certain other minor modifications.

Committee staffs indicate that additional proposals by other members are expected and that it is the House Agriculture Committee's intention to concentrate on credit questions during the early period of this session.